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E.O. 12958: DECL: 01/28/2019  
TAGS: [EFIN](#) [ECON](#) [ETRD](#) [RS](#)  
SUBJECT: KUDRIN SAYS U.S. ECONOMY KEY TO RUSSIA'S RECOVERY

Classified By: Ambassador John Beyrle, Reasons 1.4 (b/d).

¶1. (C) Summary. In a January 28 meeting with the Ambassador, Finance Minister Aleksey Kudrin said the U.S. economy's recovery would be critical to a Russian economic recovery this year. He said that policy coordination with the U.S. in particular and among G-20 countries in general would produce real benefits for the global economy and hence for Russia. Kudrin noted that the Finance Ministry was following news and changes in the Obama administration's stimulus package "online:" the GOR was revising its budget for 2009, and wanted to ensure that Russia's budget decisions coordinated with those of the U.S. He said WTO membership remained a priority, but the GOR would need to show progress toward accession within the next six months or else more protectionist groups would win the day. End Summary.

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U.S. Economy Key to Russia's Recovery  
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¶2. (C) The Ambassador told Finance Minister Aleksey Kudrin in a January 28 meeting that the new administration was developing policy themes and priorities that could shape the U.S.-Russia relationship in the coming years. The Ambassador underscored that along with strategic issues, economic issues would be at the center of the bilateral dialogue going forward.

¶3. (C) Kudrin welcomed the possibility of a renewed emphasis by the U.S. on bilateral economic ties. He said U.S. policy decisions were of critical importance to Russia's economic prospects. The world was economically interdependent, and Russia's economic recovery depended on events in other countries, above all the U.S. No recovery in Russia would occur until the U.S. began to grow again.

¶4. (C) Kudrin said he and the Finance Ministry staff monitor developments in the U.S. related to the economic stimulus package "online" (i.e. in real time). Kudrin demonstrated his familiarity with the stimulus package by sketching on a piece of paper its elements and their relative costs. He also graphed how the proposed tax cuts in the package would increase the deficit initially before leading to a period of increased revenues in a few years. Kudrin added that his staff also maintained regular contact with the Congressional Budget Office as a means of facilitating adjustments to the GOR's anti-crisis policies.

¶5. (C) Kudrin urged close coordination as the best means of emerging from the global downturn. He hoped U.S. officials would outline their economic policy goals and make

commitments on the steps to meet those goals. For example, he observed that many countries, including Russia, were considering changes in financial market regulation. Russia's economy would benefit from bilateral consultations with the U.S. to help guide the GOR's own decision-making process and ensure that they were fully coordinated.

¶6. (C) Kudrin said regular exchanges of views on financial issues and broader economic policies would also help counter domestic criticism of GOR policies, especially about the investment of Russia's foreign exchange reserves in U.S. securities. He said greater policy coordination would also facilitate a shift in future G-20 agendas from issues of general interest toward more concrete objectives. Kudrin implied he would raise this issue with Chancellor of the Exchequer Darling during his visit to London next week.

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Revising the Budget; Mitigating the Slowdown  
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¶7. (C) Underscoring his emphasis on coordination and full transparency, Kudrin spoke bluntly about his outlook for the Russian economy in 2009. His forecast for GDP growth was negative 2 percent to 0 percent, which he acknowledged was more pessimistic than the 0 to 2 percent growth his recent public comments in China had indicated. Kudrin added that the GOR was revising the federal budget for 2009 to mitigate the domestic downturn. New realities, such as lower oil prices and a lower ruble/dollar, ruble/euro exchange rate, had spurred the initiative to adjust the original 2009 budget. (Note. Kudrin's Assistant, Vadim Grishin told us earlier in the week that MinFin had not agreed to the USD 41 a barrel forecast for oil in the new budget, which it thought too optimistic. End Note.)

¶8. (C) Kudrin said the Finance Ministry's main goal in the budget revision process would be optimizing expenditures. Controlling spending was the surest way to reduce inflation and mitigate the stagflation Russia was facing. Kudrin said an increasing number of senior GOR officials recognized the need to reduce overall spending. The Finance Ministry's goal was a 2-percent of GDP reduction in the expenditures that the Duma had approved in the previous budget. Without that overall reduction, he said, the federal budget deficit would range from 5-8 percent of GDP. The Reserve Fund was large enough to cover a deficit of that size in 2009 but the GOR needed to preserve Reserve Fund resources because budget deficits were not likely to abate in the medium term; the deficit would likely be 4 to 5 percent of GDP in 2010 and would still be 3 percent in 2011.

¶9. (C) Kudrin said that although the GOR was working toward an overall spending cut, the new budget would contain additional expenditures related to the crisis. The new line items were: RUB 380 billion (USD 11.5 billion) in pension support; RUB 300 billion (USD 9.1 billion) in transfers to the regions; RUB 90 billion (USD 2.7 billion) to index certain expenditures on inflation-sensitive areas of the budget; RUB 100 billion (USD 3 billion) in additional unemployment benefits; and RUB 300 billion (USD 9.1 billion) to recapitalize the banking sector. This additional spending, Kudrin said, made it even more important to reduce spending elsewhere in the budget. Kudrin said the process of revising expenditures was ongoing and that he expected the GOR would conduct a final review of the revised budget by mid-February before sending it to the Duma.

¶10. (C) Kudrin said that in addition to optimizing and targeting expenditures, the GOR was working to stimulate the economy in a variety of other ways. One area of broad agreement within the GOR was funding banking sector recapitalization. He said the GOR had directed banks receiving state funds to increase their credit portfolios by 2 percent per month. Kudrin explained that, in keeping with this instruction, the banks were to give priority consideration to the 500-600 firms the GOR (through DPM Shuvalov's anti-crisis commission) had identified as key

recipients of support.

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WTO Membership Still Matters  
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¶11. (C) Kudrin said he, along with most other key Russian economic policy-makers, still favored Russia's WTO membership, which they believed would bring beneficial discipline to the Russian economy. However, he warned that achieving demonstrable results in the next six months would be vital for the country's accession bid. Lobbyists favoring a protectionist environment had already been busy opposing WTO accession and without significant progress, these lobbyists would become uncontrollable. He suggested that a show of support from the U.S. would help fend off these lobbyists and speed up accession.

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Comment  
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¶12. (C) Kudrin consistently has been our most transparent and realistic senior GOR interlocutor on economic issues. He has also been the most forward-leaning in seeking economic cooperation with the U.S. and other western countries. Prime Minister Putin's call in Davos for close international coordination to address the crisis and for a reliance on market solutions to the extent possible has the ring of Kudrin's influence, and thus should not be discounted as posturing. Senior officials like Kudrin and First Deputy Prime Minister Shuvalov know that Russia's economic fate is linked with ours, and they are eager to work closely and cooperatively with the new administration to restore growth to the global economy. We have a strong stake in showing our support for them, which strengthens their hand in the internal struggle with the protectionist, autarkic forces Kudrin cited in opposing WTO membership for Russia. End Comment.  
BEYRLE